VZCZCXRO9498
RR RUEHAO RUEHCD RUEHGA RUEHGD RUEHGR RUEHHA RUEHHO RUEHMC RUEHNG
RUEHNL RUEHQU RUEHRD RUEHRG RUEHRS RUEHTM RUEHVC
DE RUEHCV #0174/01 0261212
ZNR UUUUU ZZH
R 261212Z JAN 07
FM AMEMBASSY CARACAS
TO RUEHC/SECSTATE WASHDC 7609
INFO RUEHWH/WESTERN HEMISPHERIC AFFAIRS DIPL POSTS
RUCPDOC/DEPT OF COMMERCE
RUEATRS/DEPT OF TREASURY
RUEHRC/DEPT OF AGRICULTURE USD FAS
RUCPCIM/CIMS NTDB WASHDC

UNCLAS SECTION 01 OF 06 CARACAS 000174

SIPDIS

SIPDIS

STATE FOR EB/IDFD/OIA, WHA/AND
STATE PASS TO USTR
COMMERCE FOR 4431/MAC/WH/MCAMERON
TREASURY FOR KLINGENSMITH AND NGRANT

E.O. 12958: N/A
TAGS: ECON EINV EFIN KTDB STR OPIC VE
SUBJECT: VENEZUELA -- INVESTMENT CLIMATE STATEMENT (PART 2/2)

REF: 06 SECSTATE 178303

A.7. Protection of Property Rights

A.7.1. Real Property Rights

Foreign investors may pursue property claims through Venezuela's legal system. While the legal system's procedures are lengthy, judgments are uneven, allegations of corruption common, and the system itself is overtly politicized, there is little evidence that the legal system discriminates against foreign investors.

A.7.2. Intellectual Property Rights

Venezuela is a member of the World Intellectual Property Organization (WIPO). It is also a signatory to the Berne Convention for the Protection of Literary and Artistic Works, the Geneva Phonograms Convention, the Universal Copyright Convention, and the Paris Convention for the Protection of Industrial Property. Venezuela implements its obligations under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) through Andean Community Decision 486. Despite Venezuela's withdrawal from CAN in 2006, pact norms are reported to continue to be in place.

The Venezuelan Industrial Property Office (SAPI) leaves much room for improvement, and its actions and occasional publicly stated antagonism towards IPR often draw criticism from IPR advocates and rights holders. IPR protection is also hindered by the lack of adequate resources for the Venezuelan copyrigh4lA~pQQsion, including an anti-piracy law
and the introduction of a tax on street vendors. According to industry representatives, SENIAT seems to be a promising enforcement entity due to its better technical and financial capabilities.

Unfortunately, pirated software, music and movies remain readily available throughout the country. In the 2006 Annual Review, Venezuela remained on USTR's Special 301 "Priority Watch List." The Anti-contraband Law (December 2, 2005, Official Gazette 38,327) creates a framework for contraband

in Venezuelan customs which did not previously exist in Venezuela and a new Intellectual Property Rights regulation looks to enforce IPR violations in Venezuelan customs.

A.7.3. Patents and Trademarks

Venezuela provides the legal framework for patent and trademark protection through Andean Community Decision 486 and the 1955 National Industrial Property Law. Andean Community Decision 486 takes major steps towards bringing Venezuela into WTO TRIPS compliance. However, without corresponding local laws, Venezuela is not completely TRIPS compliant. Andean Community Decision 345 covers patent protection for plant varieties.

U.S. companies will continue to monitor the impact of the Andean Tribunal's 2002 interpretation of Articles 14 and 21 of Decision 486, which do not allow for the patenting of "second-use" products (e.g. new uses of previously known or patented products). Under pressure from the Andean Community and in line with some changes in leadership at SAPI, Venezuela has revoked previously issued patents. Very few patents for new pharmaceuticals were awarded in 2004 and none were issued in 2005 or 2006. Since 2002, Venezuela's food and drug regulatory agency (INH) began approving the commercialization of new drugs, which were the bioequivalent of innovative drugs that previously received INH marketing approval, thereby denying the innovative drug companies protection against unfair competition of their test data as required by TRIPS. In effect, the government now allows

unfair reliance on the test data, which required lengthy and expensive development, to be used by others seeking marketing approval for the same products.

A.7.4 Copyrights

Andean Pact Decision 351 and Venezuela's 1993 Copyright Law provide the legal framework for the protection of copyrights. The 1993 Copyright Law is modern and comprehensive and extends copyright protection to all creative works, including computer software. A National Copyright Office was established in October 1995 and given responsibility for registering copyrights, as well as for controlling, overseeing and ensuring compliance with the rights of authors and other copyright holders. Industry experts are concerned about a proposed new copyright law proposal, which would require the mandatory registry of works, reduce protection terms, hamper distribution agreements and increase royalties.

The Venezuelan copyright and trademark enforcement branch of the police (COMANPI) continues to provide copyright enforcement support with a small staff of permanent investigators. A lack of personnel, coupled with a very limited budget and inadequate storage facilities for seized goods, has forced COMANPI to work with the National Guard and private industry to improve enforcement of copyrighted material. COMANPI can only act based on a complaint by a copyright holder; it cannot carry out an arrest or seizure on its own initiative, which leads to weaker enforcement.

Venezuela does not automatically recognize foreign patents, trademarks or logotypes, so foreign investors must be sure to register patents and trademarks appropriately and in as many categories as are applicable. It is advisable not to have agents or distributors do this in their name because the agent can then claim that he/she is the registered owner of the trademark in question.

The National Assembly has also been considering a Copyrights bill for some time. The bill, which was proposed by

Venezuela's IPR regulator SAPI, has been very controversial and raised serious concerns in the private sector. Among other things, the bill calls for the local registration of all works, certification by a government-appointed commission to approve the copyright, a significant raise of royalty rates, and a provision to expropriate works if in "national interest". The new Film Law before the National Assembly is equally worrisome to the private sector, as it mandates obligatory screening of national films, higher taxation on the sector, and it requires domestic production of film equipment and copies.

A.8. Transparency of Regulatory System

A.8.1. Legal Environment

The Government of Venezuela adopted three laws in the early 1990's to promote free market competition and prevent unfair trade practices: an Anti-Trust Law (Gazette No. 34,880 of 1992), an Antidumping Decree (Gazette No. 4,441 of 1992), and a Consumer Protection Law (Gazette No. 4898 of 1995).

Venezuela also passed a government procurement law that came into effect in 2001. The law supposedly increases transparency in the competitive bidding process for contracts offered by the central government, national universities, and autonomous state and municipal institutions. Despite this legal framework, there is little transparency in Venezuela and many contracts, if not the vast majority, are awarded without open competition.

A.8.2. Tax Treatment of Foreign-Owned Firms

All companies and individuals are required to register with the national tax authority (SENIAT). Income received from

any economic activity carried out in Venezuela is subject to taxation.

Foreign companies receive equal treatment as national companies and are subject to the corporate tax regime. Except for the petroleum sector, the current Venezuelan income tax law does not differentiate between foreign-owned and Venezuelan-owned firms. The income tax rate is progressive based on income, ranging from 6 percent to 34 percent. Companies involved in hydrocarbon and related activities pay 50 percent, except associations formed under the Hydrocarbons Law, which receive a different treatment. Companies involved in mining pay 60 percent. The Business Assets Law imposes a one percent tax on business assets (Gazette No. 4654 of 1993). The assets tax is assessed on the gross value of assets (with no deduction for liabilities) after adjustments for depreciation and inflation

Venezuela has international double taxation agreements in the areas of air and sea transport with several countries, including the Unites States. A US/Venezuelan treaty to avoid double taxation went into effect on January of 2001.

SENIAT is undertaking a very aggressive tax collection program called "The Zero Evasion Plan" which has significantly boosted fiscal revenues. Highly publicized raids have taken place and businesses, including multinational firms, have been temporarily closed administratively. Firms subject to these measures complain that these closures have been imposed for minor paperwork violations as opposed to actual tax evasion.

In 1999, the government replaced the wholesale tax (ICVSM)

with a value-added tax (IVA). The value-added tax rate is currently 14 percent.

A.9. Efficient Capital Markets and Portfolio Investment

A.9.1. Capital Markets

Access to the Venezuelan secondary capital market is relatively easy, and U.S. firms essentially enjoy treatment equal to that of domestic firms. Foreign companies may issue common and preferred stocks, bonds, and other securities in Venezuelan capital markets. Foreign investors may also buy shares directly in Venezuelan companies or on the stock exchange.

The Caracas Stock Exchange (CSE) is a privately owned corporation in operation since 1947. Trading on Venezuelan stock exchanges is thin and highly concentrated. The Venezuelan Futures and Options Clearinghouse (CACOFV), the first market of its kind in the country, started operations in Caracas in September 1997. Membership in local capital markets is open to both individuals and legal entities.

A Capital Markets Law came into effect in September 1998 (Gazette No. 36,565 of 1998). It gives autonomy to the National Securities Commission (CNV) and provides regulations for intermediaries, establishes new conditions for public offerings, enhances the transparency of brokerage operations, and makes regulations more flexible for small firms that wish to issue stocks.

The Congress passed the Collective Investment Companies Law (Gazette No. 36,027 of 1996) to foster the development of Venezuela's capital market through the creation of collective investment companies. The law, which is designed to make capital market investments more attractive for small and medium investors, opened the door to the establishment of mutual funds, collective investment venture capital companies, and collective real estate investment companies. CNV issued capital requirements for collective investment companies in 1998 (Gazette No. 36,027 of 1998). The Caracas Stock Exchange (CSE) index closed above 50,000 in 2006, increasing over 155 percent from the end of the previous year. GDP growth, coupled with negative real interest rates for deposits and CDs and a lack of alternative investment opportunities largely fueled to this increase.

A.9.2. Credit Markets

The Venezuelan financial system recovered strongly from a crisis in the mid 90's that caused the failure of a number of institutions. Banks tend to register higher profits than those in other countries in the region. Much of this is attributable to exchange controls which limit the ability of the owners of capital to transfer it outside of the country. The purchase in recent years of several troubled banks by large foreign banks also injected much needed capital, technology, and competition into the sector. Foreign banks have also taken a minority interest in several other local banks. Consequently, foreign banks now control approximately 32 percent of all banking sector assets. Venezuelan banks have become increasingly dependent on the public sector as a borrower. It is currently estimated that approximately 32 percent of banks' total assets is made up of government debt.

Financing is available from a variety of sources and does not discriminate against foreign investors seeking access to credit. Banks cannot lend more than 10 percent of their

assets to any one borrower.

A major concern for the financial system is the recent legal requirement that forces banks to lend a percentage of their portfolio to specific economic sectors at preferential rates fixed by the local authorities. Thirty-one percent of commercial bank lending is directed by law to housing, agriculture, micro-business, and tourism. These loans are of concern because the mandated rates are well below market rates and below the fairly high Venezuelan inflation rate (17 percent in 2006).

A.10. Political Violence

No major incidents were confirmed against foreign-owned or operated companies, projects, or installations in Venezuela in 2006.

A.11.a. Corruption

Corruption is a very serious problem in Venezuela and appears to be worsening. According to Transparency International's Corruption Perceptions Index, Venezuela is the second most corrupt country in Latin America and one of the most corrupt in the world. Venezuela has a regulatory system to prevent and prosecute corruption and accepting a bribe is a criminal act. Penalties include fines and/or prison sentences. Historically, the country has lacked an effective judicial system to provide judicial security for either foreign or national residents. The problem persists today, and is exacerbated by the overt politicization of the judicial system. The 1999 constitution also gives the central government enhanced powers to investigate cases of corruption and oversee the use of government funds.

Government tenders are the most vulnerable to corruption because the tender process frequently lacks transparency. Critics have also targeted the current regime of government price and exchange controls as a source of corruption.

A.11.b. Bilateral Investment Agreements

Venezuela currently has bilateral investment agreements in force for the promotion and protection of investment with the following countries: Argentina, Barbados, Canada, Chile, Costa Rica, Cuba, the Czech Republic, Denmark, Ecuador, Germany, Lithuania, Netherlands, Paraguay, Peru, Portugal, Spain, Sweden, Switzerland, the United Kingdom and Uruguay. France and Belgium have signed agreements that are still awaiting legislative approval. No agreement exists with the United States.

--- -------

A.11.c. OPIC and Other Investment Insurance Programs
--- -------

OPIC currently has significant exposure in Venezuela, as does the Export-Import Bank. However, OPIC is statutorily obligated to suspend operations in Venezuela due to VenezuelaQ,s failure to achieve certification under the anti-narcotics trafficking laws. Also, the expropriations claim by SAIC to OPIC remains outstanding. Please refer to the section on Expropriations and Compensation for information on OPIC. In April 2003 Ex-Im Bank formally placed Venezuela "off cover" for new lending where it currently remains.

A.11.d. Labor

Venezuela's total labor force (all persons 15 years of age and older who are working or looking for work) was 12.5 million at the end of October 2006. According to the National Institute of Statistics (INE), 1.1 million, or 8.9 percent, were unemployed. Persons are considered as employed if they work at least 1 hour per week and INE does not count as unemployed the hundreds of thousands of Venezuelans enrolled in government social programs. Of the 11.3 million employed workers, approximately 45 percent work in the informal sector (as street vendors, domestics, small entrepreneurs, etc.). The government employs about 1.8 million of those working in the formal sector.

The major labor organizations in Venezuela are the independent Confederation of Venezuelan Workers (CTV) and the National Workers Union (UNT). The CTV was founded in 1936 and dominated the trade union movement in Venezuela prior to the election of President Chavez. The UNT enjoys support from the Venezuelan government and has been growing since its inception in 2003.

President Caldera signed landmark legislation in June 1997 (Gazette No. 5152 of 1997) to reform the outdated and unworkable severance pay system in the Organic Labor Law. The legislation was based on a framework agreement negotiated among representatives from the government, private business, and organized labor. Under the previous severance pay system, departing employees received one month's salary (two months if they left involuntarily) for each year worked based on their current pay. The 1997 system did away with "retroactivity" (i.e. basing the entire benefit on current salary) and requires employers to calculate their severance pay obligations annually and to make monthly deposits into a pension fund, an employer account, or an outside trust account. A reform in 2005 limited these payments to the equivalent of 60 percent of their annual salary.

The 1997 Organic Labor Law also provides that the minimum wage will be reviewed at least once a year and may be adjusted based on considerations such as the "food basket." A minimum wage of Bs. 512,325 (USD $238) per month took effect in September 2006.

The Organic Law Pertaining to the Integral Social Security System (Gazette No. 5199 of 1997) provides the general framework for the social security structure. Congress passed a social security reform in 1998, but the system remained under review by the Chavez government, until 2002, when the National Assembly passed the Social Security System Organic Law (Gazette No. 37600). However, the full application of this law that covers everybody that contributes or not with the expenses, will depend on the fiscal reforms.

The Organic Labor Law places quantitative and total wage cost restrictions on the employment decisions made by foreign investors. Article 27 of the Labor Law requires that the number of foreigners hired by an investor not exceed 10 percent of a company's employees, while salaries paid to foreigners may not exceed 20 percent of the total company payroll. Article 28 allows for temporary exceptions to Article 27 and outlines the requirements for hiring technical expertise when equivalent Venezuelan personnel are not available. Article 20 of the law requires that industrial relations managers, personnel managers, captains of ships and airplanes, and foremen be Venezuelan. Article 19 requires

that all orders and instructions to workers be given in Spanish.

The Venezuelan government has imposed a freeze, renewed every six months, on layoffs. Thus, reductions-in-force require the negotiation of severance packages in exchange for

voluntary resignation.

A.11.e. Foreign-Trade Zones/Free Ports

The Free-Trade Zone Law (Gazette No. 34,772 of 1991) provides for free trade zones/free ports. The three existing free trade zones are located in the Paraguana Peninsula on Venezuela's northwest coast, Atuja in the State of Zulia and Merida (but only for cultural, scientific, and technological goods). These zones provide exemptions from most import and export duties and offer foreign-owned firms the same investment opportunities as host country firms. The Paraguana and Atuja zones provide additional exemption of local services such as water and electricity. Venezuela has two free ports that also enjoy exemptions from most tariff duties: Margarita Island (Nueva Esparta) and Santa Elena de Uairen in the state of Bolivar.

A.11.f. Foreign Direct Investment Statistics

The stock of U.S. foreign direct investment (FDI) in Venezuela in 2005 was USD $9.6 billion according to U.S. Department of Commerce statistics. U.S. FDI in Venezuela is concentrated largely in the petroleum, telecommunications, manufacturing and finance sectors.

The estimated U.S. trade deficit with Venezuela for 2006 is projected at USD $30.3 billion, an increase of USD $2.7 billion from the trade deficit of USD $27.6 billion in 2005. In 2006, U.S. goods exports to Venezuela were approximately USD $8.5 billion, up USD $2.1 billion from 2005. U.S. imports from Venezuela are estimated at about USD $39 billion in 2006, an increase of USD $5 billion from the level of imports in 2005. The large increase in imports is related primarily to the increase in the price of petroleum, which represents the vast majority of U.S. imports from Venezuela.

Contacts and Web Resources

Andrew N. Bowen, Economic Counselor
U.S. Embassy, Caracas
Unit 4956
APO AA 34037
Tel: 58 212 907 8412
Fax: 58 212 907 8033
Email: BowenAN@state.gov

Darnall Steuart
Deputy Director Venezuela Desk
Office of Andean Affairs
U.S. Department of State
Tel: 202 647 4216
Fax: 202 647 2628
Email: McIsaacKJ@state.gov

Venezuela's Superintendent of Foreign Investment (SIEX):
www.siex.gov.ve.
Venezuela's Intellectual Property Rights Office (SAPI):
www.sapi.gov.ve

BROWNFIELD